No. 1146

Office - Supreme Court, U. S.
FILED
APR 14 1942
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1941.

DAVENPORT HOSIERY MILLS and UNITED HOSIERY MILLS,
Petitioners,

vs.

J. BUCKNER FISHER, Receiver of the Chattanooga National Bank,
Respondent.

PETITION FOR CERTIORARI AND SUPPORTING BRIEF.

VAUGHN MILLER,
Chattanooga, Tennessee,
Attorney for Petitioners.

MILLER, MILLER & MARTIN,
Chattanooga, Tennessee,
Of Counsel.

ST. LOUIS LAW PRINTING CO., 415 North Eighth Street. CEntral 4477.

SUBJECT INDEX.

	Page
Petition	1-7
Opinion below	1
Basis of jurisdiction	2
Questions presented	2
Summary statement of the matter involved	2
Views of the lower courts	5
Reasons for granting writ	6
1. Important question of federal law	6
2. Conflict with decisions of this Court and of other Circuit Courts of Appeal	7
Brief	8-17
I. There was no transfer of assets of the bank to defendants within the meaning of 12 U. S. C., Sections 91 and 194	8
A. Defendant's receipt and assignment of the scrip certificates constituted merely a substitution of creditors and no transfer or diminution of the assets of the bank	8
B. The "benefits" received by defendants from their use of the certificates constituted no transfer or diminution of assets of the bank	9
C. The payment by the conservator in "redemption" of the certificates was not a transfer by the bank within 12 U. S. C., Section 91	12
D. Even if the payment by the conservator constituted such a transfer, defendants did not "participate" therein	13
II. Defendants are not estopped to deny the validity of the attempted pledge of assets of the bank to secure the certificates	14
III. There is no basis for recovery of money had and received	17
Appendix (statutes involved)	19

Citations.

Ajax Shoe & Leather Co. v. Selig, ... Mass. ..., 25 N. E. (2d) 990 12
City of Marion v. Sneeden, 291 U. S. 262, 78 L. ed. 787 8
Fry v. Pennsylvania Trust Co., 195 Pa. 343, 46 A. 10.. 12
Goode v. Elwood Lodge, 160 Ind. 251, 66 N. E. 742.... 12
Granzow v. Village of Lyons, 89 F. (2d) 83.....7, 13, 15
Grubb v. General Contract Purchase Corp., 94 F. (2d) 70 .....10, 11
In re Hines, 144 Fed. 543..... 12
In re Kerlin, 209 Fed. 42..... 12
In re Lorang, 30 F. Supp. 758.....11, 12
Leonard v. Gage, 94 F. (2d) 19.....7, 13, 15
McKay v. Sperry Flour Co., 95 Wash. 209, 163 P. 377.. 12
Miller v. Fiske Tire Co., 11 F. (2d) 301..... 12
National Bank of Newport v. National Herkimer County Bank, 225 U. S. 178, 56 L. ed. 1042.....6, 10
O'Connor v. Rhodes, 79 F. (2d) 146..... 13
Olmstead v. Massachusetts Trust Co., 11 F. (2d) 410.. 12
Taylor v. R. R. Co., 86 Tenn. 228, 243..... 15
Texas & P. R. Co. v. Pottorff, 291 U. S. 245, 78 L. ed. 777 .....7, 8, 14
Security etc. Co. v. Henderson, 120 F. (2d) 449.....7, 15

Statutes.

12 U. S. C., Section 91.....12, 13, 19
12 U. S. C., Sections 91 and 194.....2, 4, 6, 8, 19
12 U. S. C., Section 203..... 13
28 U. S. C., Section 347..... 2

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1941.

DAVENPORT HOSIERY MILLS and UNITED HOSIERY MILLS,
Petitioners,

vs.

J. BUCKNER FISHER, Receiver of the Chattanooga National Bank,
Respondent.

PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals for the Sixth Circuit.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioners pray that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Sixth Circuit, entered January 15, 1942, affirming the judgment of the District Court for the Eastern District of Tennessee, Southern Division.

OPINION BELOW.

The Circuit Court of Appeals filed no opinion. Its views are indicated in a memorandum per curiam reported in 124 F. (2d) 1018, affirming the judgment "in accordance with the findings of fact and conclusions of law of the District Court."

BASIS OF JURISDICTION.

Jurisdiction is invoked under 28 U. S. C., Sec. 347.

QUESTIONS PRESENTED.

The primary question presented in this petition is whether a depositor of an insolvent national bank who receives no asset of the bank directly or indirectly, but for a consideration received from a third party assigns to the third party a part of the deposit under a certificate issued by the bank providing for such assignment and attempted to be secured by a pledge of its assets, admittedly void because ultra vires, receives a preference in violation of 12 U. S. C., Sections 91 and 194.

A corollary question presented is whether such depositor, by reason of the consideration so received from the third party, is estopped to deny the validity of such ultra vires pledge by the bank.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

These two actions were filed by a receiver of a national bank to recover certain sums claimed to have been received by petitioners (as creditors), hereinafter called defendants, when the bank was insolvent, in violation of 12 U. S. C., Sections 91 and 194. In both cases, which were consolidated for trial and appeal, judgments were awarded plaintiff, subject to counterclaims not disputed. The essential facts on the questions urged here are as follows (all dates referred to being in the year 1933):

While open on a "restricted basis" under proclamations of the President and regulations of the Secretary of the Treasury, the bank issued to defendants certificates of partial assignments, referred to in the record as "scrip certificates" or "scrip," aggregating, in face amount, in No.

2188, the sum of $18,274.00 (R. 37, 99), and, in No. 2189, $3,571.15, respectively, reading as follows (R. 61):

"5 Chattanooga National Bank 5
Chattanooga, Tennessee C 1304

"Five Dollars of a deposit in the Chattanooga National Bank of Chattanooga, Tennessee, has been assigned by the depositor thereof to the bearer hereof.

"The Chattanooga National Bank of Chattanooga has accepted this assignment and agrees to credit the account of the bearer in said bank with said amount upon the presentation hereof.

"Any credit in said bank created by presentation of this assignment to the credit of bearer is subject, at the option of said bank, to the issuance of like assignments for a period of six months from the date hereof.

Chattanooga National Bank,
W. H. DeWitt,
Cashier.

"This March 10, 1933
"5 5"

All certificates received by defendants were transferred to third parties, principally employees, in satisfaction of wage claims, and by them in turn transferred to other third parties (R. 86).

The bank attempted to pledge some of its assets to a trustee to secure the certificates (R. 36, 66-68) "under asserted reliance on Treasury Regulation No. 10" (R. 35). That Regulation (R. 43) did not confer on the bank power to make such a pledge. It authorized a national bank to the end of meeting needs of the community for food, medicines, etc., and for the payment of salaries and wages, to "exercise its usual banking functions to such extent as its situation shall permit." Regulations of the Secretary of the Treasury, promulgated March 7th and 9th, granted permission to "Clearing House Associations and other

associations organized to provide an adequately secured medium of temporary exchange" to issue certificates "to be delivered by each institution to its creditors and depositors on a pro rata basis" (R. 35, 62-64). The certificates in question were not issued by a clearing house or any other association organized to provide a medium of temporary exchange. They were originally intended to be so issued, but that plan was abandoned (R. 147-148, 165). And they were not delivered to all creditors and depositors of the bank on a pro rata basis (R. 40).

The certificates outstanding were eventually "redeemed," not by the bank, but by a Conservator for the bank under the following circumstances: On March 16th he wrote the Comptroller requesting authority to "redeem this scrip in cash" (R. 72-73). A reply authorized the redemption (R. 74), which was made (R. 38).

As respects the "circulation" of the certificates, some individuals and business establishments would accept them at face value, and others would not (R. 103-104).

Defendants denied violation of 12 U. S. C., Sections 91 and 194, because they received no asset of the bank. Their receipt and transfer of the certificates merely effected partial assignments of their deposits and thus a substitution of creditors, but no transfer or diminution of the assets of the bank. The attempted pledge to secure the certificates was void for lack of power on the part of the bank to make the pledge. The illegal "redemption" of the certificates by the Conservator was not within the scope of 12 U. S. C., Section 91, which relates only to acts of banks and not to acts of conservators, but, even if it were, it was a transaction to which defendants were strangers. The payment was a matter with which they had nothing to do and was made to third parties who received the same in their own right and were in no way related to defendants.

Views of the Lower Courts.

The District Court filed a brief opinion (R. 183-185), not reported, stating that by reason of their accepting and using the scrip certificates, "defendants are estopped to question the validity of the issuance of said scrip and the security made therefor," that they "received preferential benefits," and that "The depletion of the assets of the bank whereby the defendants were preferred is a violation of this statute, and it is immaterial in what manner the assets were depleted."

In a motion for a new trial (R. 192-195) defendants contended there was no predicate in the pleadings or the proof for estoppel. In a further opinion (p. 197) the Court expressed the views (R. 197-198): That the pledge was "illegal and invalid"; that the certificates were an attempt by a single bank "to put into circulation evidence of debt against the bank" for which "there is no statutory authority"; that defendant received the same benefit from the receipt and use of the scrip that it would have received had it been money; wherefore, "defendant has waived its right to question the validity" of the pledge to secure the scrip. It added that the parties were not "in pari delicto," because defendant was "charged with knowledge of the law" and "participated in the unlawful transactions"; and that "the whole transaction was void in its incipiency," with resulting liability on defendant "for money had and received." The Court, however, did not find or even suggest that defendants "had and received," directly or indirectly, money that had ever belonged to the bank or in which it ever had any right, title or interest.

The Circuit Court of Appeals, as shown hereinabove (p. 1), without opinion simply indicated its approval of the conclusions of law of the District Court.

REASONS FOR GRANTING WRIT.

The Circuit Court of Appeals has decided an important question of Federal law which has not been, but should be, settled by this Court.

It has decided another important question in conflict with a decision of this Court and with decisions of other Circuit Courts of Appeal.

1. Important Question of Federal Law.

12 U. S. C., Sections 91 and 194, are important statutes relating to transactions with insolvent national banks. In substance, they forbid preferential transfers by, and require a ratable distribution between creditors of, such banks. An important question here involved is whether an assignment of a claim against an insolvent bank, involving a mere substitution of creditors, in connection with which the assignor receives a "benefit" from a transaction with third parties, but no asset of the bank, constitutes a violation of those statutes. A similar question with reference to corresponding provisions of the Bankruptcy Act has been decided by this Court. In **National Bank of Newport v. National Herkimer County Bank**, 225 U. S. 178, 56 L. ed. 1042, the question was answered in the negative. No valid reason can be given for a different treatment of the statutes relating to preferential transfers by insolvent national banks. Like the corresponding provisions of the Bankruptcy Act, they speak only in terms of transfers and diminution of assets. They do not speak in terms of "benefits" received by creditors, especially where such benefits are not received at the expense of the insolvent debtor.

2. Conflict With Decisions of This Court and of Other Circuit Courts of Appeal.

The Circuit Court of Appeals has also decided a question in conflict with decisions of this Court and of other Circuit Courts of Appeal. That question is whether a party to an attempted pledge, admittedly void because ultra vires, of the assets of a national bank is estopped to deny the validity of the pledge because he has received "benefits" in connection therewith, but no assets of the bank, where none of the elements of common-law estoppel in pais are present. That question has been answered in the negative by this Court in **Texas & P. R. Co. v. Pottorff**, 291 U. S. 245, 78 L. Ed. 777, by the Circuit Court of Appeals for the Fourth Circuit in **Leonard v. Gage**, 94 F. (2d) 19, for the Seventh Circuit in **Granzow v. Village of Lyons**, 89 F. (2d) 83, and for the Ninth Circuit in **Security etc. Co. v. Henderson**, 120 F. (2d) 449.

Wherefore, it is respectfully submitted that the writ prayed for should be granted.

VAUGHN MILLER,
Chattanooga, Tennessee,
Attorney for Petitioners.

MILLER, MILLER & MARTIN,
Chattanooga, Tennessee,
Of Counsel.

BRIEF.

I.

THERE WAS NO TRANSFER OF ASSETS OF THE BANK TO DEFENDANTS WITHIN THE MEANING OF 12 U. S. C., SECTIONS 91 AND 194.

A. Defendants' receipt and assignment of the scrip certificates constituted merely a substitution of creditors and no transfer or diminution of the assets of the bank.

As appears clearly from the certificates (supra, p. 3), they were mere forms for making partial assignment of accounts at the bank. If A, having an account of $100.00 in the bank, obtained certificates for $50.00 and transferred them to B, B was simply the half owner of a claim against the bank, and his interest was identical with the half interest retained by A, viz., the interest merely of a general and unsecured creditor. Such a partial assignment in no way diminished the assets of the bank. It was merely a substitution of one creditor for another. Wherefore the issuance of such certificates to defendants, without more, of course, could constitute no violation of 12 U. S. C., Sections 91 and 194, which are designed to prevent preferential transfers and to insure ratable distribution of the assets of insolvent national banks.

The attempted pledge of assets to secure the certificates was void, as the lower courts held. It violated the principle of law that, except for purposes expressly authorized by Federal statutes, a national bank has no power to pledge its assets.

Texas & P. R. Co. v. Pottorff, 291 U. S. 245, 78 L. ed. 777;

City of Marion v. Sneeden, 291 U. S. 262, 78 L. ed. 787.

The transfer of the certificates, therefore, conferred on the transferees no right other than that of an unsecured creditor of the bank and in no way diminished its assets available for general creditors.

B. The "benefits" received by defendants from their use of the certificates constituted no transfer or diminution of assets of the bank.

1. Such benefits were not, directly or indirectly, a part of the bank's assets or anything in which it had any right, title or interest.

In using the certificates defendants obtained satisfaction of wage claims of their employees, and defendant in No. 2188 also obtained a credit to its account at another bank. But those wage claims never belonged to the bank, so that the satisfaction thereof in no way transferred or diminished its assets. Nor did any such transfer or diminution occur when defendant in No. 2188 deposited certificates at the other bank which, as assignee, simply stepped into the shoes of the assignor as an unsecured creditor. Again, it was simply a substitution of creditors.

2. Receipt by a creditor of a "benefit" not received by other creditors constitutes no transfer of assets within these statutory provisions where the bank has no right, title or interest, directly or indirectly, in or to the thing received.

So far as known, the question here involved has not been adjudicated in any reported case involving alleged preferential transfers by national banks, but in cases arising under corresponding provisions of the Bankruptcy Act the courts have consistently held that there is no preference within the inhibitions of that Act where the payment or transfer is by or with funds or property of a third person and not from the general assets of the bankrupt.

National Bank of Newport v. National Herkimer County Bank, 225 U. S. 178, 56 L. ed. 1042, was brought by the trustee in bankruptcy of Newport Knitting Company to recover from Herkimer County Bank an alleged preferential payment. The payment had been made by the Titus Sheard Company, which had indorsed paper of the knitting company and discounted it with the bank. The Titus Sheard Company was indebted to the knitting company, and, upon the insolvency of the latter, it paid and took up the paper which it had indorsed and discounted with bank, and set it off against its debt to the knitting company. In holding that the "benefit" so received by the bank did not constitute a preference, the Court, speaking through Mr. Justice Hughes, said:

> "It is not the mere form or method of the transaction that the act condemns, but **the appropriation by the insolvent debtor of a portion of his property to the payment of a creditor's claim**, so that thereby the estate is depleted."

Therein the Court affirmed a decision of the Second Circuit Court of Appeals (reversing the District Court), wherein the Court, per Judge Noyes, stated the fundamental principle as follows (172 Fed. 529, 530):

> "The one thing absolutely essential to a preference is that the bankrupt transfer some portion of his property to the creditor. If the creditor receive none of the bankrupt's property, there is no preference. And that is the primary difficulty with the complainant's case."

In **Grubb v. General Contract Purchase Corp.** (C. C. A. 2), 94 F. (2d) 70, the bankrupt, pressed by defendant creditor, arranged to meet its obligation to it by transactions attacked by the trustee as voidable preferences.

Note: All emphasis ours unless otherwise indicated.

In one instance $25,000.00 was borrowed by discounting the bankrupt's note at a trust company, the proceeds of which were placed to the bankrupt's credit in the trust company, and a check for the same amount was drawn to the trust company in exchange for a cashier's check payable to defendant. This check was delivered to defendant in exchange for collateral (which, unknown to defendant and the trust company, was forged) held by defendant as security for the bankrupt's obligation. The issues involved and contentions of defendant, which were upheld, were thus stated by Judge L. Hand (p. 72):

> "the plaintiff asserts that the case is no more than the usual one of preferences under section 60b. The defendant answers that in none of the three cases was the money ever within the bankrupt's control or a part of its assets, **and that the transactions were therefore no more than the substitution of one creditor for another without loss to the estate,** as when a surety gives money to his principal to discharge the debt. National Bank of Newport, N. Y., v. National Herkimer County Bank, 225 U. S. 178, 32 S. Ct. 633, 56 L. Ed. 1042; Bielaski v. National City Bank, 2 Cir., 68 F. (2d) 723. As to the first transaction there can be no doubt that the defendant is right."

In Re Loring (D. C. Mass.), 30 F. Supp. 758, is peculiarly in point, involving not only receipt by a creditor of a "benefit," in the form of satisfaction of the debt, but also an attempted hypothecation of assets of the insolvent in connection with the transaction. The bankrupt, indebted to defendant, entered into an arrangement with defendant and a third party whereby the bankrupt gave his note to the third party and executed a chattel mortgage on his property to secure the note, and the third party paid off the bankrupt's indebtedness to defendant. The chattel mortgage was adjudged invalid for failure to record it in compliance with the State law. The Referee held the pay-

ment a voidable preference. In vacating the order the Court said (p. 759):

> "Inasmuch as the chattel mortgage is void as to the trustee, the situation * * * is that the bankrupt, shortly before bankruptcy, gave his note to the Bushway-Whiting Ice Cream Co., the main consideration for which was the Bushway-Whiting Company's agreement to take over the indebtedness of Dutchland. The payment to Dutchland was made in compliance with that agreement. The bankrupt never had possession of the proceeds of the note, and the payment did not result in any diminution of the bankrupt's estate.
>
> "* * * such a transaction does not constitute a voidable preference. **If the mortgage had been upheld as a valid prior lien upon the assets of the bankrupt, a different conclusion might follow** * * *."

To the same effect as the three cases last above cited are **In re Kerlin** (C. C. A. 6), 209 Fed. 42; **Miller v. Fiske Tire Co.** (D. C. Minn.), 11 F. (2d) 301; **Olmstead v. Massachusetts Trust Co.** (D. C. Mass.), 11 F. (2d) 410; **In re Hines** (D. C. Pa.), 144 Fed. 543; **Fry v. Pennsylvania Trust Co.**, 195 Pa. 343, 46 A. 10; **Goode v. Elwood Lodge**, 160 Ind. 251, 66 N. E. 742; **McKay v. Sperry Flour Co.**, 95 Wash. 209, 163 P. 377; **Ajax Shoe & Leather Co. v. Selig**, ... Mass. ..., 25 N. E. (2d) 990.

C. **The payment by the Conservator in "redemption" of the certificates was not a transfer by the Bank within 12 U. S. C., Section 91.**

12 U. S. C., Section 91, which voids transfers by insolvent national banks, applies only to such transfers by the banks under the control of their own officers. It does not apply to transfers by officers or agents of the United States who have taken banks out of the hands of their own officers. It is headed:

"§ 91. Transfers **by bank** and other acts in contemplation of insolvency."

Any doubt is dispelled by the decisions that illegal transfers by receivers of assets of national banks are recoverable, not under this section, but on the common-law theory of payment by Government officers under mistake of law.

O'Connor v. Rhodes (C. C. A. D. C.), 79 F. (2d) 146;
Granzow v. Village of Lyons (C. C. A. 7), 89 F. (2d) 83;
Leonard v. Gage (C. C. A. 4), 94 F. (2d) 19, 24.

For all purposes here material conservators in charge of national banks have the same status as receivers. 12 U. S. C., Section 203.

D. **Even if the payment by the Conservator constituted such a transfer, defendants did not "participate" therein.**

1. The payment was a matter with which defendants had nothing to do.

The action of the Conservator in obtaining authority to "redeem" the certificates was independent official action on his part. His motive is indicated in his letter to the Comptroller (R. 37-38, 73):

"We * * * hope you can * * * wire us the necessary authority, as it will * * * allay the fears of the group of people who now hold this scrip, * * *."

And the Comptroller's granting of the request was likewise independent official action on his part (R. 38, 74).

2. The payment was made not to defendants, directly or indirectly, but to third parties who received the same in their own right.

All the certificates received by defendants were delivered to third parties who became the owners thereof in their own right and were free to do with the certificates

as they pleased, to tear them up, to keep them for souvenirs or to pass them to others who would take them. What they did with them was of no concern to defendants. They were not agents of or in privity with defendants. But they are the parties to whom the Conservator, without authority of law, paid the money. They are the ones who did "participate" in the illegal payment; and, whether it was a preference under the statutory provisions in question, or a payment by a Government officer under mistake of law, they are the parties whom plaintiff should have sued.

II.

DEFENDANTS ARE NOT ESTOPPED TO DENY THE VALIDITY OF THE ATTEMPTED PLEDGE OF ASSETS OF THE BANK TO SECURE THE CERTIFICATES.

The holding of the lower courts that defendants are estopped to deny the validity of the attempted pledge of assets to secure the certificates, admittedly void, is in the teeth of the ruling in **Texas & P. R. Co. v. Pottorff**, 291 U. S. 245, 78 L. ed. 777, that (p. 260):

> "The receiver is not estopped to deny the validity of the pledge. The Railway's argument is that the bank could not set up the defense of ultra vires since it had the benefit of the transaction; and that the receiver, as its representative, can have no greater right. Neither branch of the argument is well founded. **The bank itself could have set aside this transaction.** It is the settled doctrine of this Court that no rights arise on an ultra vires contract, even though the contract has been performed; and that this conclusion cannot be circumvented by erecting an estoppel which would prevent challenging the legality of a power exercised."

In that case valuable "benefits" admittedly had been received by the bank in that the pledge had relieved it of

large premiums on surety bonds for which it was substituted. But the receipt of such "benefits" was held to work no estoppel.

A similar effort to uphold, on the basis of estoppel, a pledge of assets by a national bank was made in **Granzow v. Village of Lyons** (C. C. A. 7), 89 F. (2d) 83, with respect to which the Court said (p. 85):

> "Being void, the transaction could not be confirmed, ratified, enforced or rendered enforceable by the application of any doctrine of estoppel or otherwise."

A like decision was rendered in **Security Realization Co. v. Henderson** (C. C. A. 9), 120 F. (2d) 449, 453, and in **Leonard v. Gage** (C. C. A. 4), 94 F. (2d) 19, 22.

In the case at bar a holder of the certificates was in precisely the same position as the depositors in the three cases last above cited. In each instance the attempted pledge was void, and the holder of the claim attempted to be secured by a pledge of the bank's assets was in fact the holder of nothing but an unsecured claim. In each instance benefits had been received by the party sought to be estopped. The question of estoppel in the case at bar is substantially the same question presented in the three cases cited.

The situation is controlled by the Federal statutes as construed by the Federal courts. But the same result follows from consideration of the doctrine of estoppel under the common law as applied by the Supreme Court of Tennessee. There is present none of the essential elements of estoppel in pais, which are stated in **Taylor v. R. R. Co.**, 86 Tenn. 228, as follows (p. 243):

> "Mr. Bigelow, in his very able and exhaustive work upon estoppels, upon a consideration of all the cases defining an estoppel by conduct, sums up the requisites of such an estoppel:

" 'First—There must have been a representation or a concealment of material facts.

" 'Second—The representation must have been made with knowledge.

" 'Third—The party to whom it was made must have been ignorant of the truth of the matter.

" 'Fourth—It must have been made with the intention that the other party should act upon it.

" 'Fifth—The other party must have been induced to act upon it.' Bigelow on Estoppel, 480."

With the essential elements thus outlined, to what extent, if any, are they here present?

1. What "false representation or concealment of material facts" was there by defendants?

2. What "knowledge, actual or constructive, of the facts" did defendants have that the bank or the Conservator did not have?

3. In what respect was the bank or the Conservator "without knowledge or means of knowledge of the real facts"?

4. What false representation or concealment of material facts was there by defendants with an "intention" that it be acted on by the bank or the Conservator?

5. What false representation or concealment of material facts by defendants was "relied on or acted on" by the bank or the Conservator to its or his prejudice?

III.

THERE IS NO BASIS FOR RECOVERY OF MONEY HAD AND RECEIVED.

The view that recovery might be had on the principle of money had and received was expressed by the District Court as a make-weight in its opinion on the motion for a new trial. It may be disposed of simply by pointing out (a) that defendants admittedly received nothing directly or indirectly from the bank's assets, and (b) that the action of money had and received lies only to remedy an injustice as between the parties, resulting in unjust enrichment, contrary to equity and good conscience under principles of common law (4 Am. Jur., p. 508). As between a common-law debtor and creditor (such as a bank and its depositor) it does not lie, since as between them there is no injustice in the use of the debtor's money for the benefit of the creditor, whether the debtor be solvent or insolvent. At common law there is no such thing as an illegal preference.

Respectfully submitted,

VAUGHN MILLER,
Chattanooga, Tennessee,
Attorney for Petitioners.

MILLER, MILLER & MARTIN,
Chattanooga, Tennessee,
Of Counsel.

APPENDIX.

STATUTES INVOLVED.

U. S. C., Tit. 12, §§ 91 and 194, in so far as here material:

"§ 91. **Transfers by bank and other acts in contemplation of insolvency.**

"All transfers of the notes, bonds, bills of exchange, or other evidences of debt owing to any national banking association, or of deposits to its credit; all assignments of mortgages, securities on real estate, or of judgments or decrees in its favor; all deposits of money, bullion, or other valuable thing for its use, or for the use of any of its shareholders or creditors; and all payments of money to either, made after the commission of an act of insolvency, or in contemplation thereof, made with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another, except in payment of its circulating notes, shall be utterly null and void;".

"§ 194. **Dividends on adjusted claims; distribution of assets.**

"From time to time, after full provision has been first made for refunding to the United States any deficiency in redeeming the notes of such association, the comptroller shall make a ratable dividend of the money so paid over to him by such receiver on all such claims as may have been proved to his satisfaction or adjudicated in a court of competent jurisdiction, and, as the proceeds of the assets of such association are paid over to him, shall make further dividends on all claims previously proved or adjudicated;".

(23)

(Office - Supreme Court, U. S.)
FILED
MAY 8 1942
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 1146.

DAVENPORT HOSIERY MILLS AND UNITED HOSIERY MILLS,
Petitioners,

v.

J. BUCKNER FISHER, RECEIVER OF THE CHATTANOOGA NATIONAL BANK, *Respondent.*

RESPONSE TO PETITION FOR CERTIORARI.

PHIL. B. WHITAKER,
Attorney for Respondent.

WHITAKER & WHITAKER,
Of Counsel.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

SUBJECT INDEX

Page

Statement of the Case 1

Reasons Assigned in Petition for Granting Writ..... 6

Questions Presented by the Petition..... 7

The "Primary" Question..... 7

"The primary question presented in this petition is whether a depositor of an insolvent national bank who receives no asset of the bank directly or indirectly, but who, for a consideration received from a third party, assigns to the third party a part of the deposit under a certificate issued by the bank providing for such assignment and attempted to be secured by a pledge of its assets, (admittedly void because ultra vires), received a preference in violation of 12 U. S. C., Sections 91 and 194."

The "Corollary" Question..... 12

"A corollary question presented is whether such depositor, by reason of the consideration so received from the third party, is estopped to deny the validity of such ultra vires pledge by the bank."

Conclusion 22

CASE CITATIONS

Ball v. German Bank, 187 Fed. 750..... 9

Browne v. Stronach, 7 F. (2d) 685 9

Federal Reserve Bank v. Omaha National Bank, 45 F. (2d) 511 9

Hirning v. Federal Reserve Bank, 42 F. (2d) 925..... 9

National Bank of Newport v. National Herkimer County Bank, 225 U. S. 178.....6, 16, 18, 22

National Security Bank v. Butler, 129 U. S. 223..... 9

Second National Bank of Toledo v. M. Samuel & Sons, 12 F. (2d) 963 16

Smith v. Baldwin, 69 F. (2d) 390..... 9

Page

Texas & P. R. Co. v. Pottorff, 291 U. S. 245, 78 L. Ed. 777 6
Vann v. Federal Reserve Bank, 47 F. (2d) 786..... 9

STATUTE CITATIONS.

Sec. 91, Title 12, U. S. C.....6, 7, 8, 12, 22
Sec. 194, Title 12, U. S. C. 6, 7

MISCELLANEOUS CITATIONS.

21 C. J. 1206 14
41 C. J. 12 12
41 C. J. 17 13
Restatement of the Law on Restitution, sec. 48..... 17

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 1146.

DAVENPORT HOSIERY MILLS AND UNITED HOSIERY MILLS,
Petitioners,

v.

J. BUCKNER FISHER, RECEIVER OF THE CHATTANOOGA NATIONAL BANK, *Respondent.*

RESPONSE TO PETITION FOR CERTIORARI.

STATEMENT OF THE CASE.

This suit was brought by the Receiver of the Chattanooga National Bank, an insolvent national banking corporation, against the defendants, (who are depositors of said bank), for allegedly excessive withdrawals constituting an illegal preference to these defendants, the withdrawals having been made during the so-called banking holiday of 1933 proclaimed by the President of the United States. The Chattanooga National Bank will be referred to herein as the "Bank"; the Davenport Hosiery Mills, Inc., and the United Hosiery Mills, as the "Mills."

The Bank closed its doors as of the close of business for the day, on March 1, 1933, pursuant to a proclamation of the Governor of Tennessee, and did not thereafter reopen for regular banking business. (R. 31 and 32)

From March 1, 1933 until 3:00 a.m. on the morning of March 14, the officers and directors of the Bank were feverishly, and valiantly attempting to make arrangements to reopen the Bank in anticipation of the expected expiration of the banking holiday proclaimed by the President on March 6th. Its cash position was not good. Efforts were made to obtain loans, both from the Reconstruction Finance Corporation and from the Federal Reserve Bank, but the commitments which these institutions made were not as large as the officers and directors hoped they might be. Nevertheless, the Bank did make application for a license to reopen (R. 26), which application was granted, and a license accordingly issued. (R. 27) After a careful review of the entire situation, however, the executive committee of the Bank, at 3:00 a.m., March 14, the date when it was authorized to reopen, decided to recommend to the directors that the Bank not reopen, and that a Conservator be appointed. (R. 54-57) Z. C. Patten, a director of the Bank, was appointed Conservator (R. 59) and served until November 6, 1933, when Paul J. Kent was appointed Receiver. (R. 34 and 35) These suits were originally instituted in the name of the Receiver, Kent, but were later revived in the name of his successor, J. Buckner Fisher. (R. 186)

Believing that the Bank would reopen on March 14, it was open upon a restricted basis from March 10 to March 13, inclusive, in asserted reliance on Treasury Regulation No. 10 (R. 43), during which time it cashed four checks of petitioner, Davenport Hosiery Mills, totaling $18,574.65, by paying scrip of the face value of $18,274.00 and cash in the amount of $300.65. (R. 35, 36, 37) Copies of the checks totaling the above amount are filed as Exhibits. (R. 69, 70 and 71) In the case of the United Hosiery Mills it was stipulated that if respondent was entitled to recover anything the amount was $892.79, which is the amount of the

checks cashed by it, less dividends retained by respondent. (R. 86)

The dates from March 10 to March 13, 1933, inclusive, were the only dates that the Bank was open for any purpose from the time it closed on March 1 until the Conservator was appointed on March 16, and on these dates the Bank was open only for the purpose of transacting such business as was authorized by the said Treasury Regulation No. 10. The substance of Treasury Regulation No. 10, in so far as it applies to this case, is that Banks whose financial situation permitted them to do so might exercise their usual banking functions to meet the needs of the community for food, medicine and other necessities of life, for the relief of distress and for the payment of salaries and wages, etc. The Regulation further provided that no bank should engage in any transaction which was violative of any Federal Law or of any order issued by the Comptroller of the Currency. The scrip which the Bank issued to these petitioners when it cashed their checks reads as follows:

> "Chattanooga National Bank,
> Chattanooga, Tennessee.
>
> Five dollars of a deposit in the Chattanooga National Bank of Chattanooga, Tennessee, has been assigned by the depositor thereof to the bearer hereof. The Chattanooga National Bank of Chattanooga has accepted this assignment and agrees to credit the account of the bearer in said bank with said amount upon the presentation hereof. Any credit in said bank created by presentation of this assignment to the credit of bearer is subject, at the option of said bank, to the issuance of like assignments for a period of six months from the date hereof.
>
> This March 10, 1933.
>
> (Signed) Chattanooga National Bank,
> W. H. DeWitt, Cashier" (R. 61).

At a meeting of the Directors on March 9, 1933, the Bank was authorized to issue scrip and the officers of the Bank were authorized to pledge assets of the Bank as security

for the redemption of scrip (R. 64, 65, 66). On the following day,—March 10, 1933,—the Bank executed a trust agreement, under the terms of which it transferred and assigned to the First National Bank of Chattanooga as Trustee securities belonging to the Bank of the face value of $250,097.69. The instrument provided that the said securities were pledged for the purpose of fully satisfying in cash the scrip which the bank was to issue. The First National Bank of Chattanooga accepted the trust and acknowledged receipt of the securities totalling $250,097.69. (R. 66, 67 and 68)

J. H. Davenport, President of the Davenport Hosiery Mills, (Cause No. 2188), **was also a director of the Bank,** and attended and participated in the Bank's directors' meeting which authorized this unlawful pledge of the Bank's assets. (R. 105, 107, 108 and 65) The public, through the press, was advised that the payment of the scrip was amply secured and that it would be redeemed in cash at its face value. (R. 172, 173, 174, 175, 176)

When these securities were taken out of the general assets of the Bank and pledged to the First National Bank of Chattanooga as Trustee for the purpose of securing the redemption in cash of all scrip issued by the Bank only to those depositors who could qualify under the provisions of Treasury Regulation No. 10, while all other depositors and creditors of the Bank did not enjoy this privilege, an illegal preference was then and there extended to these depositors, including these petitioners. This transaction enabled these petitioners to pay their obligations to their employees out of the assets of the Bank when the Bank had already committed an act of insolvency while the Bank was insolvent.

When the petitioner Davenport Hosiery Mills received the scrip from the bank, after presenting its checks therefor, *it paid all of it to its employees with the exception of $2,751.62 at the full valuation of one hundred cents on the dollar,* and these employees traded this scrip to merchants or other parties whom it is impossible to identify. The

$2,751.62 was deposited by this defendant in the American Trust & Banking Company, which bank treated the deposit as a cash deposit (R. 100, 101 and 102).

The same is true of petitioner, United Hosiery Mills, except that no portion of the scrip it received was deposited, but all of it was paid to its employees at one hundred cents on the dollar, who in turn traded it to merchants or other parties in Chattanooga, treating the scrip as cash (R. 86).

During the dates from March 10 to March 13, inclusive, the Bank issued scrip in the face amount of $117,989.00, of which $18,274.00 worth was issued to petitioner Davenport Hosiery Mills, and a smaller amount was issued to the United Hosiery Mills. Since the issuance of the scrip, the Bank has redeemed all of it in cash with the exception of scrip of the face value of $199.00, but for the redemption of this the Receiver now holds a special account in the sum of $199.00 in cash (R. 37, 38).

Out of the $199.00 of scrip which has not been redeemed, the Bank issued $106.00 to Sam H. Carter upon the presentation of his check therefor and this amount the said Sam H. Carter destroyed (R. 88-92).

It results, therefore, that scrip having a face value of $93.00 is unaccounted for out of the total amount of $117,989.00 issued by the Bank. The facts are that these petitioners have never been called upon to make good any of the scrip issued to them which they, in turn, either paid to their employees, or deposited in another bank, both the bank and the depositor treating it as cash.

By this circuitous and illegal arrangement, these petitioners have been able to obtain assets from the bank, which other depositors were unable to obtain. When called upon to make restitution by paying back an amount sufficient to place themselves on the same basis with other depositors, they refused.

REASONS ASSIGNED IN PETITION FOR GRANTING WRIT. (Pet. 8)

We submit that in this case the Circuit Court of Appeals has decided no new question of law. It has merely reiterated the established law that a bank after committing an act of insolvency shall not prefer one creditor over another.

We submit that the decision of the Circuit Court of Appeals in this case *is not only not in conflict with, but, on the contrary, is in complete harmony with* the reasoning and the conclusions of law laid down by this Court in *National Bank of Newport* v. *National Herkimer County Bank*, 225 U. S. 178, 56 L. Ed. 1042. We will fully discuss this case on subsequent pages of this brief.

We also submit that there is no conflict between the decision of the Circuit Court of Appeals in this case and the decisions of other Circuit Courts of Appeal in the cases cited on page 7 of the petition. Nor is there a conflict with the decision of this Court in *Texas & P. R. Co.* v. *Pottorff*, 291 U. S. 245, 78 L. Ed. 777. The question of the preference of one creditor over another in the distribution of the assets of a national bank in violation of Section 91 and Section 194 of Title 12, U. S. C. was not the controlling issue in these cases. All of said cases deal with a bank's pledge of its assets to secure a deposit while the bank was amply solvent, and long before the commission of an act of insolvency. The pledges were declared void because *ultra vires*. In the instant case the pledge was "utterly null and void" because violative of Section 91, Title 12, U. S. C.

This National bank has been in liquidation for more than nine years. The remaining assets have been sold and final relief can be given depositors as soon as pending litigation is completed. There is no public interest in the questions presented and there is no conflict in decisions to be resolved. The parties had their day in court when their rights were resolved by the two courts below.

The issues presented, and the type of transaction involved, are peculiar to the unusual conditions then existing, and no general administrative policy relating to the liquidation of national banks is presented.

QUESTIONS PRESENTED BY THE PETITION.
(Pet. 2)

The two questions presented by the petition, one referred to as primary and the other as corollary, are as follows:

> "The primary question presented in this petition is whether a depositor of an insolvent national bank who receives no asset of the bank directly or indirectly, but who, for a consideration received from a third party, assigns to the third party a part of the deposit under a certificate issued by the bank providing for such assignment and attempted to be secured by a pledge of its assets, (admittedly void because ultra vires), received a preference in violation of 12 U. S. C., Sections 91 and 194.
>
> A corollary question presented is whether such depositor, by reason of the consideration so received from the third party, is estopped to deny the validity of such ultra vires pledge by the bank."

THE "PRIMARY" QUESTION.

It will be noted that the "pledge of assets" by the Bank is referred to as "admittedly void because ultra vires." Rather was this pledge "utterly null and void" because violative of the express provisions of Section 91, Title 12, U. S. C., and because the pledge of assets and assignment of interests therein by these petitioners prevents and makes impossible a "ratable dividend" to be paid to all creditors as required by Section 194 of the same Title.

The petitioners attempt to split into separate transactions the single transaction evidenced, first, by the Bank's illegal pledge of certain of its assets to redeem in cash the scrip which it issued and, second, the issuance of the scrip itself.

It is impossible to split this single transaction into two separate transactions. One is dependent on the other. Each is an integral part of the other. The issuance of the scrip was authorized at a meeting of the Board of Directors held March 9, 1933, and the Minutes of the meeting show that authority was then granted for the issuance of the scrip and the officers were then authorized to pledge definite security

for the payment of the scrip, which security was taken from the general assets of the Bank (R. 65).

The trust indenture by which the officers and directors attempted to secure the scrip and the scrip itself were both dated March 10, 1933. The securities delivered by the Bank to the First National Bank had a face value of $250,097.69, and the trust indenture provides that the scrip should be paid in cash (R. 67).

This effort of petitioners to split the single transaction into separate transactions, stripping the admittedly illegal portion from what petitioners contend is legal, results in their whole argument being based upon a false premise. A house built upon the sand cannot stand.

Section 91, Title 12 U. S. C. (R. S., Sec. 5242), provides as follows:

> "All transfers of the notes, bonds, bills of exchange, or other evidences of debt owing to any national banking association, or of deposits to its credit; all assignments of mortgages, sureties on real estate, or of judgments or decrees in its favor; all deposits of money, bullion, or other valuable thing for its use, or for the use of any of its shareholders or creditors; and all payments of money to either, made after the commission of an act of insolvency, or in contemplation thereof, made with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another, except in payment of its circulating notes, shall be utterly null and void; and no attachment, injunction or execution, shall be issued against such association or its property before final judgment in any suit, action, or proceeding in any State, county, or municipal court."

The object of this statute is plain. It is to prevent a national bank from preferring one creditor over others under the following circumstances:

(a) After the commission of an act of insolvency;

(b) In contemplation of insolvency;

and with a view to

(1) Preventing pro rata application of assets to the satisfaction of claims of depositors and creditors. Federal Reserve Bank v. Omaha National Bank, 45 Fed. (2d) 511; Brown v. Stronach, 7 F. (2d) 685; Smith v. Baldwin, 69 Fed. (2d) 390, or

(2) Preference of one creditor over another. Ball v. German Bank, 187 Fed. 750; National Security Bank v. Butler, 129 U. S. 223; Hirning v. Federal Reserve Bank, 42 F. (2d) 925; Vann v. Federal Reserve Bank, 47 Fed. (2d) 786.

The petitioners' position is that when they presented their checks and obtained therefor only scrip instead of cash, there was no transfer of assets, no depletion of the assets of the bank, no payments made to defendants, that the certificates were simply partial assignments of accounts in the bank and since the attempted pledge to secure the payment of the scrip was void, the petitioners received only certificates which they could transfer to others who would have to take their chances on the amount of cash which they finally received for the certificates.

The petitioners take this position in spite of the fact that the record shows without dispute that they presented their checks to the bank made out for a certain number of dollars and received therefor scrip in dollar denominations of an amount equal to the amount of the check and that thereafter they treated the scrip as cash, paid it to their employees, whom they persuaded to accept it as cash in full discharge of the employees' claim against the Mills for services rendered, and in spite of the fact that thereafter the employees treated it as cash and paid it to merchants treating it as cash; that the scrip continued to circulate as cash and was finally redeemed by the Bank in cash. At the same time, the public was assured by the Bank through the press and through editorial comment that the scrip "was as good as greenbacks".

To show clearly how the Bank regarded the scrip, we quote the following from a letter of March 16, 1933, to the

Deputy Comptroller of the Currency from Z. C. Patten, Conservator of the Bank. Mr. Patten was a director of the Bank. After referring to the issuance of the scrip, he stated:

> "Due to the uncertainties of the general situation, and realizing that if *cash* were paid for these purposes, much of it would have been hoarded and shipped out of town, the local banks decided to issue scrip instead of *paying out the cash*. However, in order to insure the free circulation of the scrip, the local banks agreed that each of them would *definitely secure it* and our attorneys stated that in view of the fact that we had been authorized to pay *cash*, that such security would be valid, as it was the nature of a loan, to be used for an emergency, and to prevent *the use of actual cash*. For the most part, the scrip went into the hands of wage earners and small salaried people, much of it finding its way into the hands of small retailers and will work a tremendous hardship upon a large number of people if the bank were not permitted to redeem it in cash." (Italics inserted.)

Thereupon he further states that the scrip was secured by "well-selected good notes", which were delivered to the First National Bank, Trustee. Thereupon, he also asks authority to redeem the scrip in cash and obtain the return of the security from the trustee (R. 72-73). *All of the foregoing was afterwards done.*

If the Bank had issued cash to the petitioners instead of adopting this circuitous arrangement,—in which the President of the petitioner Davenport Hosiery Mills actively participated as a director of the Bank,—there could be no denial of the depletion of the assets of the Bank. It is not denied that these petitioners have received benefits which other depositors less fortunately situated were not able to obtain. But the condition of the Bank at this time was such that it was afraid to deplete the relatively small amount of cash which it had on hand by paying those depositors in cash who presented checks for payrolls, etc. At this time, the Bank still hoped to reopen on March 14th and

hoped to obtain loans from the Reconstruction Finance Corporation or the Federal Reserve Bank in an amount sufficient to justify reopening. Therefore, the Bank devised the scheme of issuing scrip in lieu of cash. But in order to give the scrip the quality of a circulating medium at its full face value, the Bank depleted its assets to the extent of $250,097.69 by pledging securities of this value to the First National Bank as Trustee for the express purpose of fully satisfying in cash the scrip which it issued.

It is a fundamental rule of law that that which is illegal, if done directly, cannot be made legal by indirection. When the defendant presented its checks and obtained scrip therefor, which recited on its face

> "$1.00 of a deposit in the Chattanooga National Bank of Chattanooga, Tennessee, has been assigned by the depositor thereof to the bearer hereof",

and passed this scrip on to its employees at a full valuation of one hundred cents on the dollar, *it was not thereby attempting to assign an interest in its deposit as this deposit existed on March 1st*,—when the Bank was last open for business,—*but it passed on to the employees an interest in its deposits, which to the extent of the amount of scrip issued had become a secured deposit*—or, to more accurately state it, it was a deposit that the Bank had attempted to secure illegally—illegal, among other things, for the reason that the Bank had already committed acts of insolvency, and because the Bank was then insolvent and was attempting to give to these depositors advantages in the race for assets which other depositors not so fortunately situated could not enjoy.

A proper legal interpretation of the terms of the scrip certificates cannot be reached by a mere examination of the scrip itself. On the contrary, the scrip must be read and interpreted in the light of the trust indenture entered into with the First National Bank, under the terms of which the redemption of the scrip at its full face value in cash was assured.

THE "COROLLARY" QUESTION.

The petitioners deny that the principles of estoppel are involved in this case, and also that there is any basis for recovery of money had and received. These questions are discussed on pages 14 and 17, inclusive, of the petition. We will answer these questions together.

Section 91 of Title 12 classifies as "utterly null and void" all transfers of the notes, etc., of any national bank made after the commission of an act of insolvency, or in contemplation thereof and with a view to preventing the application of its assets in the manner prescribed by the Statute, or with a view to the preference of one creditor over another. It results, therefore, that the transfer of the securities to the First National Bank for the redemption of the scrip in cash was utterly null and void. The assignment of the defendant's interest in its supposedly secured deposit also becomes utterly null and void and therefore the holder of the scrip who presented it to the Bank for payment and who received payment at one hundred cents on the dollar, obtained, in the final analysis, money for the benefit of the petitioners, inasmuch as the petitioners profited out of this illegal transaction by satisfying their debts in full at the expense of other creditors of the Bank.

> " 'Money paid' is a phrase used as equivalent to the phrase 'money paid by one for the use or benefit of another to a third party.' " *41 C. J. 12.*

Continuing the same text says:

> "One who has paid money for the use and benefit of another to a third party may recover from that other the money so paid, if such payment was made at that other's express request, or if he subsequently ratified it, or if, in the absence of such request or ratification, it was made under circumstances from which the law will imply an obligation to repay, even though there was no express promise to repay, the law implying such a promise. Where there is no request and the obligation to repay is implied solely in law, such obligation is said to be founded on a constructive contract or quasi con-

tract. Where there is an express request, or a ratification, the right of recovery is founded on contract, and is governed by the ordinary rules applicable to contracts implied in fact; nevertheless, since it is customary in common-law pleading to declare on such a payment in the same language as is used to declare on a payment made without such request, or indeed against the wish of defendant, such payment is commonly regarded as being embraced under the phrase 'money paid' and is here so treated."

In the instant case, the Bank in effect entered into a contract with the petitioners to issue scrip to it upon the presentation of its checks for pay rolls, and agreed to redeem the scrip in cash at their full face value, having prior thereto attempted to pledge its securities to the First National Bank for the redemption of the scrip.

"One who, under a contract subsequently rescinded or found unforceable, has made, for the benefit of the other contracting party, payments or disbursements to a third party, may recover such payments from the other contracting party." *41 C. J. 17.*

The implied contract between the Bank and the petitioners was unenforcible for the reason that the Bank, having prior to this time committed acts of insolvency, was not permitted legally to transfer its asssets as security for the payment of the scrip.

The implied contract for the redemption of the scrip in cash is evidenced by the face of the scrip itself. The concluding sentence of the scrip, after reciting that the Bank agrees to credit the account of the bearer in the Bank with the amount of the scrip upon presentation, is as follows:

"Any credit in said bank created by presentation of this assignment to the credit of bearer is subject, at the option of said bank, to the issuance of like assignments for a period of six months from the date hereof."

The only conclusion to draw from this language is that if the Bank did not exercise the option during the six months

period, it would redeem the scrip in cash during the period. At the end of the six months period the Bank had no option except to pay it in cash. The terms of the scrip itself, therefore, put the petitioners on notice that the Bank was agreeing to redeem the scrip in cash. In harmony with this provision on the face of the scrip is Paragraph 2 of the trust indenture entered into with the First National Bank:

> "The credits given upon the presentation of said certificates (scrip) may, at the option of said bank, during the period of six months from March 10, 1933, be satisfied by the issue of similar certificates and said securities are pledged as security that the final credits given for said certificates will be fully satisfied in cash."

Although this transaction is believed to be void in so far as creditors of the Bank are concerned, and in so far as any rights or obligations under the transaction are involved, yet the existence of this transaction as a factual circumstance under which payment was made in this case and the fact that payment was made pursuant to this arrangement and that the effect of this arrangement was a payment pursuant to the direction and request of the depositor made for his benefit, cannot be denied by the depositor inasmuch as the depositor accepted the benefits of the transaction and directed and permitted the Bank to make payments pursuant thereto. The depositor cannot, under these circumstances, repudiate the effect of this transaction which was to give it a preference.

It is said in 21 C. J. 1206:

> "Where one having the right to accept or reject a transaction takes and retains benefits thereunder, he ratifies the transaction, is bound by it and cannot avoid its obligation or effect by taking a position inconsistent therewith."

The petitioners in their brief insist that there can be no elements of estoppel in this case because the Bank knew as much as the defendants did with reference to the transaction. P. 15 and 16. This is not a contest between the

Bank and the petitioners, but it is a contest between the creditors of the Bank, represented by the Receiver, and the petitioners.

Certainly it cannot be claimed that the large number of creditors who were not permitted by the Bank to make withdrawals as these petitioners did were in any sense a party to these illegal transactions. They had no knowledge of the arrangements which the Bank had made for the benefit of the favored few.

As stated by the trial judge:

> "It is to be remembered that this contest is not between two parties in pari delicto. * * * The defendant in its transaction with the Bank was charged with a knowledge of the law and the rights of creditors in case of insolvency.
>
> "It results that on the one side we have the creditors who are innocent of wrongdoing and on the other side we have the defendant who participated in the unlawful transaction. Hence, the application of the doctrine of estoppel. Cf. Joy v. Godchaux, 35 Fed. (2d) 649.
>
> "The court is of the opinion that the doctrine of estoppel or waiver is the true rule for determination of this case. But if estoppel or waiver did not apply, the whole transaction was void in its incipiency and the defendant would be liable for money had and received." (R. 199)

It cannot for a moment be doubted that the real beneficiaries of this entire transaction were the petitioners. They owed bills to employees which normally would have been paid in cash. Cash was not available from the Bank. But the Bank worked out this arrangement whereby scrip (the payment of which in cash, at a later date, at its full value, was secured), would be accepted by the petitioners' employees *in lieu of cash*. It was so accepted. It passed from hand to hand as a medium of exchange. It was presented to the Bank and redeemed in cash at its full value. The parties who redeemed it are not now subject to identification. The petitioners stand as the unquestioned benefici-

aries of the entire arrangement. It is immaterial in the last analysis whether the petitioners received cash for their checks or received scrip, for the redemption of which, in cash, arrangements had already been made.

In *National Bank of Newport* v. *National Herkimer County Bank*, 225 U S. 178, Justice Hughes, later Chief Justice, said:

> "To constitute a preference, it is not necessary that the transfer be made directly to the creditor. *It may be made to another for his benefit.* If the bankrupt has made a transfer of his property, the effect of which is to enable one of his creditors to obtain a greater percentage of his debt than another creditor of the same class, *circuity of arrangement* will not avail to save it. A 'transfer' includes 'the sale and every other and different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security.' It is not the mere form or method of the transaction that the act condemns, but the appropriation by the insolvent debtor of a portion of his property to the payment of a creditor's claim, so that thereby the estate is depleted and the creditor obtains an advantage over other creditors." (P. 184)

In *Second National Bank of Toledo* v. *M. Samuel & Sons*, 12 Fed. (2d) 963, it is said:

> "From the days of Lord Mansfield's decision in Moses v. Macferlan, 2 Burr. 1065, 97 Eng. Reprint 676, decided in 1760, the common-law courts have recognized the right to sue in the equitable action of indebitatus assumpsit to recover money paid by mistake, or if 'the defendant upon the circumstances of the case is obliged by the ties of natural justice and equity to refund the money'. And as stated in Mr. Woodward's work on Quasi Contracts, Sec. 3, quasi contractual obligations are defined as 'arising without reference to the assent of the obligor, from the receipt of a benefit the retention of which is unjust, and requiring the obligor to make restitution.' 'They rest solely upon the universally recognized moral obligation

of one who has received a benefit, the retention of which would be unjust, to make restitution.' Id., Sec. 6".

"The defendant has entered into no contract with the plaintiff herein. The contract appears to have been with the Irving National Bank, which issued the letter of credit. The defendant procured the Irving National Bank to issue the letter of credit, and it, and not the defendant, was therefore, the promisor. While no contractual relation exists between the plaintiff and the defendant, the defendant has assumed a quasi contractual relation with the plaintiff. That relationship grows out of the fact that the defendant received a benefit the retention of which would work a serious injustice to the plaintiff. And this quasi contractual obligation is imposed without reference to the obligor's assent. It is essential to the existence of a quasi contractual obligation that it be shown: (1) That the defendant has received a benefit from the plaintiff. (2) That the retention of the benefit by the defendant is inequitable." (P. 967)

Assuming it to be true that no specific contract existed between the petitioners and the Bank, certainly it cannot be denied that the necessary elements of a quasi-contractual obligation existed. The petitioners,—as the result of the scheme devised by the Bank,—have unquestionably received the benefit of discharging in full the claims of their employees. The retention of this benefit unquestionably is inequitable and unfair because it gives these petitioners an advantage over other depositors, all of whom the respondent represents.

The petitioners should be required to make restitution for the unlawful advantage which they have obtained over other creditors. The Restatement of the Law, in the Volume on Restitution, at page 196, Sec. 48, says:

"Unless otherwise agreed and except as stated in Sec. 52, a person is entitled to restitution for a benefit which he has conferred upon another as the whole or part of his performance of a contract with another, under the erroneous belief induced by a mistake of law, either shared by both or known to the other, that the manifested basic purpose of the contract can be carried

out or is thereby achieved. If the purpose fails in part and the benefit is severable, there can be restitution pro tanto."

In reply to the narrow view which is taken of respondent's substantive rights with respect to a preference, we wish further to discuss the case of *National Bank of Newport* v. *National Herkimer County Bank*, 225 U. S. 178, and its proper application to the case at bar.

In that case the National Herkimer County Bank was a creditor of the Newport Knitting Company by reason of a note upon which the Titus Sheard Company was secondarily liable as an endorser. The Titus Sheard Company paid the National Herkimer County Bank in full and claimed subrogation, or reimbursement, from the bankrupt Newport Knitting Company. To effect this claim for reimbursement the Titus Sheard Company set up on its books a debit in its favor upon an account which it owed to the bankrupt, this debit being in the full amount of its payment to the National Herkimer County Bank, and the bankrupt, Newport Knitting Company, set up a corresponding credit in favor of the Titus Sheard Company. These two bookkeeping entries were made without the knowledge of the National Herkimer County Bank, which was the creditor to whom the alleged preference was made.

The Trustee in Bankruptcy of the Newport Knitting Company sued the National Herkimer County Bank, claiming that the setting up of the credit in favor of Titus Sheard Company was an intermediate step in the granting of a preference to the National Herkimer County Bank, which was paid in full by Titus Sheard Company. The theory of the Trustee in Bankruptcy was that the credit in favor of the Titus Sheard Company was a depletion of the assets of the bankrupt, and that this depletion of the bankrupt's assets indirectly resulted in the benefit to the National Herkimer County Bank through the payment which was made to the Bank by the Titus Sheard Company in exchange for the credit in its favor against the bankrupt.

The Court held that since the Titus Sheard Company had acted on its own behalf, and that there was no arrangement between the bankrupt and the National Herkimer County Bank for indirectly paying the National Herkimer County Bank by means of the credit to Titus Sheard Company—the National Herkimer County Bank, in fact, knowing nothing at all about any depletion of assets of the bankrupt's estate —the National Herkimer County Bank could not be construed to have received a preference.

The payment to the National Herkimer County Bank by the Titus Sheard Company was for the purpose of relieving the Titus Sheard Company of its endorsement liability to the National Herkimer County Bank. The National Herkimer County Bank could have collected this from Titus Sheard Company, regardless of whether the Titus Sheard Company received any reimbursement from the bankrupt.

The Court said that the preference was in the setting up of the credit to Titus Sheard Company, and that this credit should be rescinded, which would then leave the estate of the bankrupt in exactly the same condition that it was before the credit was set up.

The Court further said, however, that if there had been an arrangement between the bankrupt and its creditor, the National Herkimer County Bank, to prefer the National Herkimer County Bank by means of a credit to Titus Sheard Company which was to have been transferred to the National Herkimer County Bank, then, notwithstanding the "circuity of arrangement", the Trustee in Bankruptcy might have recovered the preference from the National Herkimer County Bank. The statement of the Court on page 184 is as follows:

> "if an insolvent debtor arranges to pay a favored creditor through the disposition of such an account, to the depletion of his estate, it must be regarded as equally a preference, whether he procures the payment to be made on his behalf by the debtor in the account—the same to constitute a payment in whole or part of the latter's debt—or he collects the amount and pays it over to his creditor directly."

It is submitted that the hypothetical case of Justice Hughes is analogous in principle to the present case. This hypothetical case contemplated a situation where the bankrupt should agree with its creditor, the National Herkimer County Bank, to prefer it by paying assets to a person indebted jointly with the bankrupt to the National Herkimer County Bank, which debtor would, in turn, pay the debt of himself and the bankrupt to the National Herkimer County Bank, thus paying off the National Herkimer County Bank's claim against the bankrupt in full.

In the case at bar the Chattanooga National Bank agreed, in effect, with the Davenport Hosiery Mills and the United Hosiery Mills, that it would pay them in cash in advance of its other creditors, by paying the employees of these companies, but these payments were only to be made to such employees of the Mills as should first pass the benefit on to the Mills by discharging their claims against the Mills.

The difference between this case and the hypothetical case supposed by Justice Hughes is that in the hypothetical case the assets of the insolvent are delivered to the third person with a mere agreement that the third person would discharge the insolvent's debt to his creditor in full, whereas in the case at bar the parties did not trust the third party to that extent; they required that the third party first discharge the insolvent's liability to his creditor and then come and get the cash.

To phrase the problem in another way, we may say that the Chattanooga National Bank gave to the Davenport Hosiery Mills and the United Hosiery Mills a *power* to realize in full upon their deposit claims against the Bank. This power was to be exercised by designating a creditor of the Mills to whom the Bank agreed to pay cash. The Bank's agreement to pay cash was secured by a pledge of its assets.

We do not see that it is material whether the bank fulfilled its obligation to pay the persons designated by the Mills before or after the Mills reaped the benefit of the exercise of this power. Since the entire transaction was carried out

pursuant to an original written agreement to give a preference of which the Mills were to reap the benefit, the ultimate consummation of this agreement to give a preference must be related to the original agreement of which it was merely the conclusion.

This original agreement to give a preference clearly shows that the creditor of the Bank who was to receive the scrip and use it to discharge his indebtedness was the beneficiary of the ultimate cash payment then agreed to be made. The execution of the illegal agreement was in accordance with its terms and intent, and the defendants actually received the intended benefit therefrom.

The curious reasoning of the petitioners is that it was unlawful for the Mills to receive the benefit that they derived from this illegal agreement. Therefore, say the petitioners, the court should conclude that the benefit received by them was void, and, therefore, they did not receive any benefit, and, therefore, respondent has no cause of action against petitioners.

According to this line of reasoning, since all preferential transfers are void, they are non-existent and no suits of any kind could ever be predicated upon them. We respectfully submit that if preferential transfers and liens are "void", it is a character of voidness which can only be taken advantage of by the creditors of a bank for whose benefit they are made void. A preferred creditor can hardly be heard to rely upon the illegality of the preference to support his protestations that he received nothing. Nor should he be heard to say that payments of cash made to others pursuant to a lien given by the Bank for his benefit were not in fact made pursuant to such lien because no such lien ever existed, it being declared void by statute.

We submit that the word "void" as used in the statute means "void as to creditors", not void as to the person receiving benefits under the voided transaction.

The petitioners also seek to take advantage of the fact that the pledge of assets by the Bank was *ultra vires* apart

from insolvency. We doubt if under any circumstances the petitioners would be in a position to take advantage of the *ultra vires* character of the act. Certainly, they could not do so and retain the benefits of the transaction which they are attacking.

CONCLUSION.

In its final analysis the position of the petitioners is this: They admit that the scheme under attack in these suits, devised by the Bank after the commission of an act of insolvency, and while insolvent, inured directly to their own benefit. The petitioners admit that a portion of the scheme, —that is, the pledge of the assets to the First National Bank, Trustee, to secure the payment of the scrip,—was illegal, but, say the petitioners, "We had a perfectly legal right to assign all or any portion of our deposit to any third person and, having this right, this portion of the transaction should stand stripped of the illegal pledge of assets." But it was not this type of assignment that these petitioners attempted to make. The assignment which they attempted to make was an assignment of an interest in their deposit secured by the pledge of assets to the extent of the assignments. It was one single illegal transaction, directly violative of Section 91 of Title 12, U. S. C., and classified by this Section as "utterly null and void".

The petitioners can hardly deny that if their checks presented to the bank had been paid all in money instead of mostly in scrip and partially in money, they would be forced to make restitution. We submit there is no difference in principle between the withdrawal of money and the withdrawal of assets having an equal or greater money value.

As said by Chief Justice Hughes in *National Bank of Newport* v. *National Herkimer County Bank, supra*, "circuity of arrangement will not avail to save it."

Respectfully submitted,

PHIL B. WHITAKER,
Attorney for Respondent.

WHITAKER & WHITAKER,
Of Counsel.